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ABSTRACT

The federal-state system of unemployment insurance (UI) in the United States was established by the Social Security Act of 1935 during the Great Depression. Under the program, states provide temporary partial wage replacement to involuntarily unemployed workers with significant labor force attachment. The federal government induced states to establish UI programs through two means: (1) a uniform federal tax imposed on employer payrolls, with a 90 percent reduction granted in states operating approved UI programs, and (2) grants to states to administer their programs. The system has evolved into a collection of separate state programs adapted to different regional, economic, and cultural contexts that all satisfy the same broad federally set standards. This paper reviews state practices concerning applicant eligibility, benefit generosity, and benefit financing, with the aim of revealing lessons for a possible European unemployment benefit system (EUBS). We examine areas of federal leadership, explicit federal-state cooperation, and state innovation. While the U.S. system offers some good ideas for setting up an EUBS, there are also lessons in some shortcomings of the U.S. experience. We overview existing UI systems in European countries and review the debate on EUBS within the European Union. We identify areas of risk for individual and institutional moral hazard in a multi-tiered UI system and give examples of monitoring methods and incentives to ameliorate such risks. We suggest approaches for gradual system development, encouraging lower-tier behavior, benefit financing, and responses to regional and system-wide crises.

JEL Classification Codes: J65. H81, H87

Key Words: unemployment insurance, European unemployment benefit system, multi-tiered system, moral hazard, incentives, public finance

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Given the uneven experience across European nations during the Great Recession with programs to temporarily replace lost income during involuntary unemployment, the European Union (EU) has renewed interest in a multinational system of unemployment insurance (UI) within the European Monetary Union (EMU).[1] Concerns about ensuring adequate protection for unemployed workers, along with political tensions about the potential international spillover effects unemployment can have between nations on the continent, has focused the effort to find models for cooperation between member nations. Because of its long history and two-tier structure, the federal-state UI system in the United States has emerged as a possible model for a European Unemployment Benefits System (EUBS).

While there has been prior debate within the EU about introducing an EUBS, such a scheme does not exist. However, the crisis of the Great Recession exposed shortcomings of some national UI systems within the EMU, and the topic has reemerged. Some leaders are clearly in favor of an EUBS, while others have rejected the idea. A recent large opinion survey of European citizens in thirteen member states indicates majority support for international sharing of unemployment risk insurance through modest but adequate income transfers across countries (Vandenbroucke et al. 2018). The survey suggests Europeans favor UI that provides adequate income replacement while emphasizing job training, education, and reemployment assistance.

In this paper we review aspects of the two-tiered UI system operating in the United States as a prime example for international cooperation within the EU. We examine US provisions for UI applicant eligibility, benefit generosity, and benefit financing, with the aim of revealing

[1] For the United States, the National Bureau of Economic Research business-cycle dating committee set the official length of the contraction starting in December 2007 at 18 months. It was the longest U.S. contraction since the Great Depression, which started in August 1929. The Great Recession earned its name not only from its length but from the speed of decline following the evaporation of credit, the permanence of high-wage job loss, and the international ripples it caused, which are still being felt (Grusky, Western, and Wimer 2011).

lessons for a possible EUBS. We examine areas of federal leadership, explicit federal-state cooperation, and state innovation. While the US system offers some good ideas for setting up an EUBS, there are also lessons in some shortcomings of the US experience.[2] We identify areas of risk for individual and institutional moral hazard in a multi-tiered UI system and give examples of monitoring methods and incentives to ameliorate such risks. After examining aspects of the US system, we describe the history of the EUBS debate, designs that have been considered, and the future outlook for an EUBS. We conclude by summarizing a plan based on US experience for gradual EUBS development, encouraging specific behaviors by EU member countries, promoting benefit financing cooperation, and giving elements of a plan to respond to regional and system-wide crises.

1. Background on the American System

The federal-state US unemployment insurance (UI) program was established by the Social Security Act of 1935 to provide temporary partial wage replacement to involuntarily unemployed persons actively seeking new jobs. A federal incentive to create state UI programs was provided by a tax incentive. A federal unemployment tax was imposed on wages paid by UI-covered employers with a 90 percent reduction in the federal tax granted to employers in states establishing UI systems in conformity with federal guidelines.[3] The tax revenue accruing from the 10 percent retained by the federal government is used for grants to states for program administration, funding public employment services (PES) operated by the states, paying the

[2] Other recent papers drawing lessons for European nations considering adopting a multi-tiered UI system are Fischer (2017) and Lenaerts, Paquier, and Simonetta (2017).

[3] Title III of the Social Security Act established federal grants to the states to perform administrative functions for UI, and Title IX established the federal unemployment tax and related provisions (Blaustein 1993, pp. 151–153). The federal tax rebate incentive for states to establish UI programs was found to be constitutional by the Supreme Court in 1937 (Blaustein 1993, pp. 157–158).

federal share of benefits under the permanent extended benefits program, providing support for federal expenses incurred in operating the UI and employment service functions, and making loans to pay regular benefits when state reserves are inadequate. Federal law provides states with the latitude to establish practices that adapt to the economic and cultural conditions in that state. The interplay of federal and state partners has resulted in a system that varies greatly at the state level but maintains important federal standards nationwide.

There are five main goals for the federal-state UI system: 1) to provide temporary partial wage replacement during involuntary unemployment, 2) to prevent dispersal of employers' workforces during temporary layoffs, 3) to promote rapid return to work, 4) to limit business downturns by maintaining aggregate purchasing power, and 5) to encourage stabilization of employment in enterprises through experience rating (O'Leary and Straits 2004). The experience rating feature of UI tax contribution rates means that tax rates are higher for employers with more benefit charges, and vice versa. Experience rating is a financing feature of UI that is unique to the United States. In addition to acting as an incentive to stabilize employment, it is intended to increase employer involvement in monitoring UI eligibility, as well as by making employers aware that layoffs have consequences for their tax rate.[4] Over the 80-year history of the program, the objectives were largely met during the first 40 years, but, as discussed below, many program elements have eroded since the 1980s.

The original benefit provisions in most state UI laws were modest, whereas financing features tended to be more than sufficient. In 1936, the federal taxable wage base of $3,000 was high enough so that 95 percent of all wages paid in the country were subject to the 3 percent

[4] Fath and Fuest (2005) summarize research evidence that experience rating stabilizes employment when it is effective in the United States. However, state taxable wage base limits, tax rate maximums, and solvency taxes limit the range of experience rating and the effectiveness of employment stabilization.

federal tax rate. The high coverage and modest tax rate led to the rapid accumulation of reserves in state accounts. Ten years after program establishment, system-wide reserves were over 10 percent of total wages in UI-covered employment (USDOL 2015). The accumulated reserves led to improved benefit levels and longer potential durations. By the 1970s, benefits typically replaced 50 percent of lost wages up to the state maximum weekly benefit amount for up to 26 weeks of involuntary unemployment.[5] Today, the financial foundation for UI is weaker, and benefit provisions have been reduced in many states.

2. Evolution of Federal Rules for State UI Conformity[6]

The existing federal-state UI system is a delicate balance of power that was designed to be self-regulating by a built-in incentive structure. The federal partners hold the upper hand in the relationship. That is because federal requirements for conformity and compliance are central to regulating the system (Table 1). In other words, state UI laws must conform to federal law or pay a much higher tax, and actual state practice must comply with federal regulations.[7]

The Social Security Act of 1935 provided 12 minimal conformity requirements. Two requirements were added about the use of UI-granted funds during the early 1940s. New federal laws in the 1950s required coverage to be broadened, resulting in additional requirements, and more new requirements were added in 1970 and 1976. In recent years, an overriding federal concern has been controlling federal spending; consequently, changes to the UI system have often been done as part of the budget reconciliation process, because the federal Unemployment

[5] A similar pattern of modest beginnings with improved financing and benefit adequacy over time can be observed in newer UI programs among many countries in Latin America (Summit of the Americas Center 2003).

[6] This description was extracted and updated from O'Leary and Straits (2004).

[7] As listed in *Code of Federal Regulations*, Title 20, Chapter 5, Parts 601–625. www.gpo.gov/fdsys/ accessed July 24, 2017.

Trust Fund (UTF) is treated as part of the unified federal budget, even though the states raise all the money for supporting their state UI systems.

Table 1 A Chronology of Increasing Federal Conformity Requirements for State Unemployment Insurance Systems in the United States

Original conformity requirements set in 1935 were minimal. They said states must:

- Make full payment of benefits when due
- Make benefit payments through public employment offices
- Have a fair appeals hearing process
- Transfer tax receipts immediately to the Unemployment Trust Fund (UTF)
- Use withdrawals from the state account in the UTF only to pay UI benefits
- Make required reports to the US Secretary of Labor
- Provide information to any federal agency running public works or assistance
- Not deny benefits to eligible individuals
- Not pay benefits until two years after contributions start
- Not deny benefits for refusal to fill a vacancy resulting from a labor strike
- States may repeal their UI laws at their own discretion
- Additional employer rate reductions must be based on experience rating

Additional federal requirements were added in the following years regarding:

- Interstate claims rights
- Rules for combining earnings from multiple employers to gain entitlement
- Broadened coverage of employers
- Allowing claimants receiving approved training to be eligible for UI
- Requirement that states must participate in the Extended Benefits (EB) program
- Denial of benefits to workers who are not legal residents with employment privileges

More federal requirements in later years regard:

- Intervening work required for requalification
- Denial to professional athletes during the off-season
- Benefit reduction for public pension income

Restrictions motivated by the desire to conserve funds in the federal budget:

- The Unified Budget Act of 1969 added the Unemployment Trust Fund to the annual federal budget.
- Federal eligibility requirements for extended benefits were adopted.
- The Balanced Budget and Emergency Deficit Control Act of 1985 was passed.
- New claimants were profiled to identify those most likely to exhaust benefits, and they were required to participate in ES.
- States were required to make withholding of federal income tax possible for beneficiaries.

A chronology of conformity requirements is given in Table 1. The original requirements covered prompt payment of benefits, location where UI payments were to be received, appeals procedures, management of funds, reporting to the US Department of Labor, and the requirement of experience rating as the basis for receiving the 90 percent reduction in FUTA tax rates. Requirements added in the 1940s and 1950s were included mainly to simplify procedures when interstate claims were involved. In more recent years, states have complained that federal conformity requirements have become more specific and their value more questionable, such as the requirement that professional athletes not be covered in the off season.

3. Program Standards

Conformity standards govern many aspects of state program design, but other elements, including the amount and duration of benefits, are left to state choice. The following summary relies on recommendations issued by two federal advisory bodies, the 1980 National Commission on Unemployment Compensation and the 1996 Advisory Council on Unemployment Compensation.

3.1. Eligibility

Unemployment insurance in the United States is regarded as social insurance, having elements of both private insurance and social welfare. Eligibility rules are set to reduce individual moral hazard by requiring applicants to meet three criteria: 1) be involuntarily jobless because of an unavoidable job separation; 2) have sufficiently strong recent attachment to the labor force; and 3) be able, available, and actively seeking work. The greatest variation among states is in the difference in the level of recent income required to qualify for UI benefit eligibility. Some states require as little as $1,000 over the prior base year, while others require as much as $5,000. To accommodate administrative systems, the base year is normally defined as the first four of the past five completed calendar quarters.

3.2. Generosity

The standard of benefit adequacy accepted in the research literature is 50 percent wage replacement for up to six months, with a maximum benefit amount equal to two-thirds the average wage in covered employment (ACUC 1996). These levels were common among states by the 1960s and for more than 50 years thereafter, but in response to the UI debt accumulated by states during the Great Recession, eight states have retreated from these common levels of benefit adequacy (USDOL 2018).[8] In the United States, there are no fixed federal requirements for duration or the dollar amount of weekly payments.

3.3. Financing: FUTA and SUTA

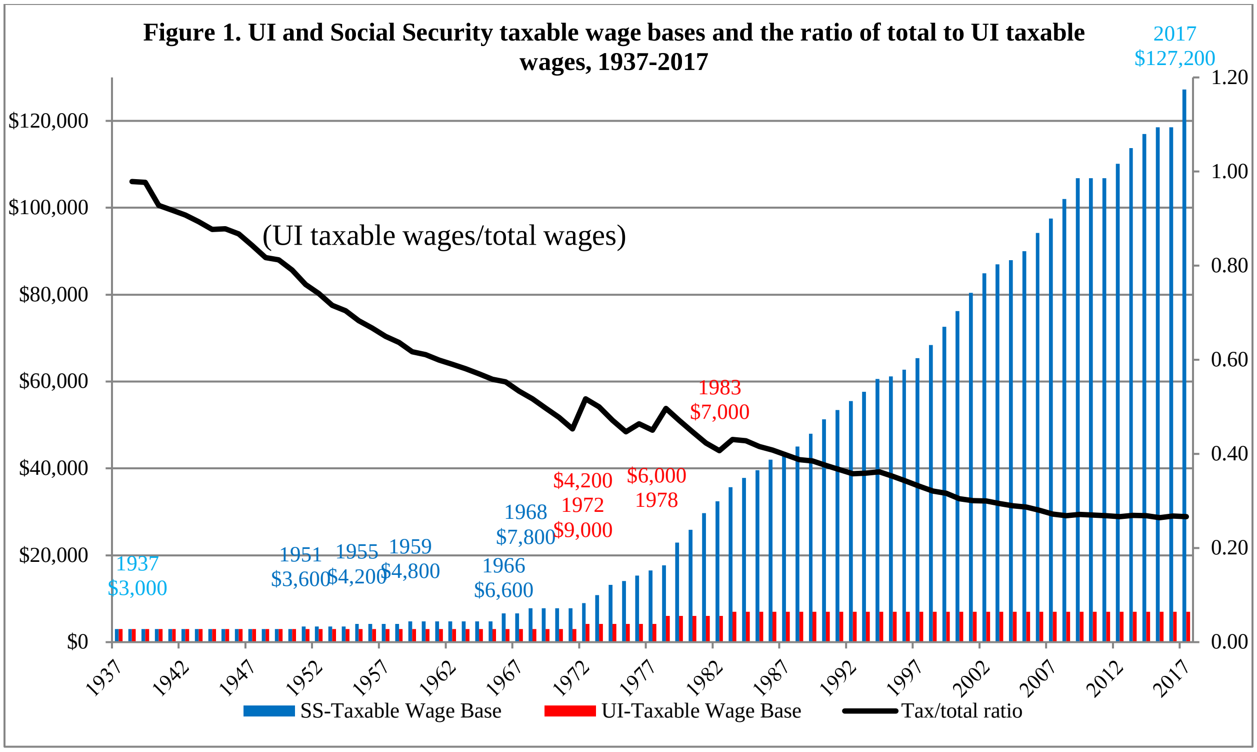
Since 1951, the Social Security taxable wage base has risen dramatically, while the UI taxable wage base has stagnated (Figure 1); since 1977 legislation, the Social Security taxable wage base has been indexed to average wages, while the FUTA wage base has no automatic adjustments The FUTA taxable wage base also is the minimum taxable wage standard for states.

Since 1939, the FUTA tax base has been increased only three times; most recently it reached $7,000 in 1983. The FUTA taxable wage base now stands at less than 6 percent of the Social Security taxable wage base. In 1937, more than 95 percent of all wages and salaries in UI-covered employment were subject to the FUTA tax, but by 2015, only about 25 percent were subject to the FUTA tax (O'Leary and Kline 2016). All states must have state tax rates that are at least 90 percent of the FUTA levels before reduction, and they must have taxable wage bases

[8] The eight states with UI potential duration of less than 26 weeks as of January 1, 2018 are Arkansas, Florida, Georgia, Illinois, Michigan, Missouri, North Carolina, and South Carolina.

that are at least at the FUTA level. Two state taxable wage bases are at the federal minimum of $7,000, and more than half are less than double the FUTA base. The stagnant tax base has contributed to insufficient buildup of reserves to forward-fund benefits, which has resulted in adverse distributional consequences and tax incidence.

Figure 1. UI and Social Security taxable wage bases and the ratio of total to UI taxable wages, 1937-2017



Sources: USDOL (2019), O'Leary and Kline (2016).

As noted above, debt from insufficient forward funding induced eight states to reduce potential benefit durations. The limited tax base may also dampen hiring of low-wage workers, for whom employers pay a relatively larger share of total annual compensation in UI taxes. The ACUC (1996) recommended incentive approaches for inducing states to forward-fund benefits. Recommendations included paying increasing interest rates on higher positive-balance reserves above an adequate minimum. Vroman (2016) asserts that UI financing systems operate best when kept in balance with benefit systems. That is, if the maximum benefit amounts are indexed to average wage levels, then the taxable wage base should also increase along with wage increases.

4. Areas of Explicit Federal-State Cooperation

4.1. Permanent Federal-State Extended Benefits Program

The Extended Unemployment Compensation Act of 1970 created a permanent program for UI extended benefits (EB) to be paid when the insured unemployment rate (IUR) exceeded set trigger levels.[9] The EB program involves a 50-50 sharing of benefit payment costs between federal and state governments. When triggered, the EB program lengthens potential durations by 50 percent of the entitled duration of regular UI benefits. In most states, that means an additional 13 weeks of benefits after the entitlement to regular UI is exhausted.[10] Benefits under EB are paid at the same weekly rate as regular UI. The EB program paid benefits in recessions in several states during the first 10 years after enactment, but it has rarely been triggered since that time.

Originally, the EB program was a good example of federal-state cooperation. However, in recent years the triggers based on insured unemployment have rarely activated EB when total unemployment rises (Nicholson and Needels 2006). Under the original 1970 law, EB could be activated by a national trigger affecting all states, or a state-level trigger affecting EB only in that particular state.[11] In the early 1980s, the national trigger was eliminated and the state IUR trigger

[9] The IUR is the rate of insured unemployed persons in a period as a percentage of the UI-covered employed persons in the period. This ratio depends on the rate of UI application, the rules for benefit eligibility, and the enforcement of eligibility rules.

[10] States can opt to add an additional 25 percent of the regular potential duration to the EB duration.

[11] The original triggers set in 1970 were a national trigger of 4.5 percent IUR over 13 weeks that would activate EB for all states, and a state-level trigger of 4.0 percent IUR over 13 weeks that was at least 120 percent of the IUR in the same period one year earlier.

threshold was raised from 4 to 5 percent (Woodbury and Rubin 1997).[12] Additionally, increasing UI eligibility requirements in some states resulted in low UI recipiency rates and low IUR rates that failed to trigger EB even when the total unemployment rate (TUR) had risen to quite high levels (Blank and Card 1991). In response to the failure of EB to be activated in more than a few states during the early 1990s recession, in July 1992 Congress passed legislation allowing states to adopt an alternative trigger based on the total unemployment rate (TUR).[13]

In the 1990s and 2000s, emergency federal UI extensions were structured to be paid before any EB that might be available. Consequently, the EB program has not actively functioned in the past 40 years. During the Great Recession, the American Recovery and Reinvestment Act (ARRA) provided temporary 100 percent federal reimbursement of EB payments for states that adopted alternative EB triggers based on the TUR. The 100 percent payment for EB was continued through midyear 2014 for states with conforming TUR triggers. All states that adopted TUR triggers had active EB programs during the Great Recession, but a survey of states revealed that almost all TUR adopters said they would return to IUR triggers after the 100 percent federal funding ended (Mastri et al. 2016).

4.2. UI performance measurement

The Government Performance and Results Act of 1993 (GPRA) requires each executive branch agency to do four things: 1) establish performance goals for each program activity, 2) express the goals in measurable form, 3) describe the operational process, and 4) establish performance indicators. The UI performance measurement system monitors administrative performance (rates for 2015) including: rate of timely payments (83.7 percent), rate of detecting

[12] The Ninety-Sixth Congress included the changes in PL 96-364 and PL 96-499 in 1980 and 1981.

[13] The 1992 UI reforms were included in PL 102-182. The threshold for the alternative state EB trigger was a TUR above 6.5 percent over a three-month period and 10 percent above the three-month average TUR in either of the two preceding years.

recoverable overpayments (61.2 percent), and rate of employer tax liability determinations (87.3 percent).[14] UI Performs also tracks one program outcome measure: the reemployment rate for UI claimants (67.7 percent)—based on quarterly wage records in program administrative data.

4.3. Reed Act Distributions

Originally, employer FUTA tax payments were recorded as general revenues of the US government, and UI administrative expenses were paid for out of general revenues. By the early 1950s, it was estimated that FUTA revenues exceeded UI administrative grants to states by between $500 million and $1 billion annually (West and Hildebrand 1997). The Employment Security Administrative Financing Act of 1954 requires that any excess amount of FUTA revenues over UI administrative grants to states be deposited to the UTF in a new account to make loans to states when their reserves were insufficient to pay UI benefits. The financing act, commonly called the Reed Act, set a limit on the level of reserves in the loan account and provided that reserves above that ceiling level be distributed to states for payment of regular benefits, program administration, or delivery of PES services.[15] Over time, the Reed Act ceilings became less binding as Congress, motivated by the desire to control annual deficits in the unified federal budget, relaxed the Reed Act ceiling trigger from 0.33 percent of total payrolls in UI covered employment in 1982 to 1.02 percent of covered payrolls today (Vroman 2008). Consequently, the incentive supplied by the Reed Act for Congress to adequately appropriate money from the UTF for UI administration has diminished. Nonetheless, the Reed Act mechanism is an important example of a mechanism for maintaining balance in a decentralized federal-state system.

[14] A summary of these main UI performance targets and results can be found at http://www.oui.doleta.gov/unemploy/docs/GPRA_Summary_Report.asp accessed July 25, 2017.

[15] The 1954 law (P.L. 83-567) became known as the Reed Act after its sponsoring representative, Daniel A. Reed of New York.

5. Area of State Innovation

5.1. Bond Financing of Benefit Payment Debt

An alternative to forward-funding is pay-as-you-go financing of benefits. By keeping employer UI taxes low, states will likely see declining reserve balances when unemployment rises, but they keep money in the hands of private-sector businesses, where jobs are created. In today's low-interest-rate environment, UI benefit payment debt can be financed by tax-exempt state revenue bonds at interest rates far below the lending rates available from the federal government. Under Title XII of the Social Security Act, states with insufficient reserves can borrow from the US Treasury. Currently the Title XII lending rate is 2.23 percent, while rates on state revenue bonds are below 0.5 percent.[16] Some states have adopted the pay-as-you-go model, which is a rational cost-saving approach in a low-interest-rate environment. However, this will not always be the case. When rates eventually rise, and the spreads between Title XII loans and tax-exempt state revenue bonds shrink or flip, forward-funding will regain appeal.

6. Areas of Federal Leadership

6.1. Holding State Reserves for Payment of Benefits

The Social Security Act requires that all employer UI tax payments be deposited into the Unemployment Trust Fund (UTF) at the US Treasury. The FUTA contributions paid on federally taxable payrolls are deposited into the Employment Security Administrative Account (ESAA) in the UTF. Additionally, states are required to promptly deposit revenues from their state unemployment tax act (SUTA) levies into state accounts in the UTF. The US Treasury pays

[16] Current Title XII loan rates can be found at www.treasurydirect.gov/govt/reports/tfmp/tfmp_advactivitiessched.htm accessed April 20, 2019.

interest on positive reserve balances in state accounts and charges interest on loans to states from the Treasury, except for short-term cash-flow borrowing in any year that is paid back by September 30 of that year.

6.2. Financing State Program Administration

The federal-state relationship has been greatly affected in recent years by the federal budget implications of state actions. Federal grants to states for UI administration are determined by a formula based on workload factors such as the number of UI claims, appeals, and covered employers. Driven by tight budgets, the federal government has tried to conserve funds, while the states have claimed that federal holdings for administration are state entitlements that should be distributed. Davidson and Martin (1996) argue that to encourage high-quality service, efficient low-cost administration, and continuous quality improvement, the administrative funding mechanism should 1) be based on the quality of services delivered, and 2) that states should retain unspent financial grants.

6.3. Incentive for States to Forward-Fund Benefits

For a state UI system to be sustainable in the long run, revenues should match expenditures, on average, over business cycles. The accepted standard for UI benefit financing is based on the principle of forward-funding. Having money in reserves when unemployment increases means states do not have to raise employer UI taxes during recessions. Therefore, forward-funding reduces or eliminates any UI tax increases that could drive the economy into a worse situation when business conditions are weak. Accumulating reserves during economic recoveries puts a slight damper on expansions but helps avoid severe financing crises in the depths of recessions.

To achieve adequate forward-funding, state accounts in the federal Unemployment Trust Fund (UTF) should maintain balances “sufficient to pay at least one year of unemployment insurance benefits at levels comparable to its previous high cost" (ACUC 1996, p. 11). In 2010, this rule was put into place as a federal requirement for interest-free loans. The rule requires states to hold one year of reserves in the UTF equal to the average of the three highest-cost rates experienced in the prior 20 years. This rate is known as the average high-cost rate (AHCR). The rule becomes fully effective in 2019; in 2014, it started to be phased in at a target rate of 50 percent of the AHCR and increases of 10 percentage points each year until it reaches the AHCR in 2019.

6.4. Loans to States to Pay Benefits

Most states that exhaust their reserve balance use the normal UI benefit financing procedure for loans available from the US Treasury under Title XII of the Social Security Act. Funds available for loans to states are accumulated from the annual FUTA tax levy that all UI-covered employers pay. As mentioned in the previous subsection, adequate forward-funding means zero-interest short-term loans will be available, but states must pay interest charges on loan balances that remain outstanding after September 30 in any given year. The interest rate moves in tandem with yields paid in the market for US Treasury bonds. For example, rates since 2008 have ranged from 4.94 percent down to 2.23 percent.[17]

A total of 36 states borrowed from the US Treasury between 2009 and 2013. "By the end of 2015, 10 states still had outstanding loan or bond debts. Four state UI programs (California, Connecticut, Ohio, and the US Virgin Islands, which is counted as a state) are still paying on loans from the US Treasury, while six other states (Colorado, Illinois, Michigan, Nevada, Pennsylvania, and Texas) are still repaying other loans or bond debts from UI benefit payments" (O'Leary and Kline 2016, p. 1). In terms of systemic risks to the loan fund, Vroman (2012, p. 4)

[17] U.S. Treasury loan rates can be found at https://www.treasurydirect.gov/govt/rates/rates_tfr.htm.

finds that “the largest states seem likely to be among the last to fully repay their UI loans.”

6.5. Discretionary Emergency Extensions of Benefits

Since the 1950s, the federal government has provided emergency unemployment compensation (EUC) every time the annual average national unemployment rate has risen above 6 percent. There have been eight EUC-type programs, each enacted at congressional discretion, and all completely or mostly funded by general revenues of the federal government. During the Great Recession, the program EUC08 was first enacted in 2008 and subsequently revised and extended several times; the last updates were in 2012. At its peak, the combination of EUC08 and EB provided up to 73 weeks of benefits on top of 26 weeks of regular UI. To be eligible for funds from EUC08, beneficiaries must have exhausted regular state UI. No EUC08 benefits were paid after January 2, 2013.

Economic theory suggests that longer potential UI duration can induce longer benefit receipt (Decker 1997). Some scholars suggest this happened in the 2008–2012 period, when generous EUC was available with longer durations; however, others find no evidence that EUC affected the rate of leaving insured unemployment (Farber, Rothstein, and Valletta 2015). In addition to partially replacing lost income, UI also aims to help stabilize the macroeconomy and arrest the descent into poverty by the unemployed. Yang, Lasky, and Page (2010) of the Congressional Budget Office (CBO) assessed the timeliness and cost-effectiveness of 11 macroeconomic stimulus measures. They rated EUC the most effective because of a large income multiplier, and because EUC is a one-time expenditure that does not add to the nation’s structural deficit. A related CBO analysis by Acs and Dahl (2010) found that among households in 2009 with at least one member of the household unemployed, those receiving EUC08 had a poverty rate of 19.6 percent, while the poverty rate of those same households would have been 24.3 percent without EUC.[18]

In addition to EUC08 extending UI benefits during the Great Recession, the ARRA of 2009 provided for Federal Additional Compensation (FAC) to increase all UI weekly benefit amounts by $25 a week through June 30, 2010, at a cost of $9 billion. This FAC was subsequently extended to December 31, 2010. The ARRA also provided 65 percent subsidies for up to 12 months of extended health insurance premiums for UI-eligible persons who had lost their jobs on or after September 1, 2008.

6.6. Mentoring State Program Administrators

The US Department of Labor, together with the National Association of State Workforce Agencies (NASWA), mentors new state UI program administrators and state program management staff. In most cases, the chief state UI administrator is a political appointee who serves for a limited time. However, the legal responsibilities of the position are real, and the decisions that must be made often carry great weight. In 2015, the US Department of Labor published a manual for state administrators titled "Unemployment Insurance Directors Guide." The manual provides a comprehensive summary of the program and the director's responsibilities. In addition to general annual conferences on workforce development, NASWA hosts annual UI directors' conferences. Additionally, the US Department of Labor has well-established mechanisms for documenting regulations that are contained in the *Federal Register*, reviewing state proposed legislative changes for federal conformity, and publishing occasional program letters announcing available grants and program changes. Annual events are scheduled for training state staff in areas of program emphasis, including financial forecasting of reserve

[18] Acs and Dahl (2010) did not consider behavioral response to longer potential UI durations, but it must be recognized that labor demand was exceptionally weak throughout 2009.

balances and updating WPRS profiling models. The resources available to state directors and their administrative staffs are well developed and continuously improving.

6.7. UI Modernization under ARRA[19]

The American Recovery and Reinvestment Act (ARRA) of 2009 provided financial incentives for expansions of UI eligibility that together were referred to as "UI modernization." The available financial incentives totaled $7 billion. States could receive one-third of their potential incentive payment for having an alternate base period (ABP) available for monetary determination of UI eligibility that includes the most recently completed calendar quarter, and the remaining two-thirds for having any two other benefit liberalizations.[20]

By the end of grant availability on June 30, 2011, 41 states had received modernization payments for having an ABP, and 36 of these states also received the remaining two-thirds of their available funds. However, since that time some states have repealed some or all of the expansions of UI eligibility adopted to qualify for modernization payments.[21]

6.8. Special Unemployment Benefits Programs

The federal government funds and administers special unemployment benefit programs for Disaster Unemployment Assistance (DUA) and Trade Adjustment Assistance (TAA). Applicants for these must qualify for UI benefits under regular state programs, and benefits are funded by the federal government. There are special eligibility rules in disaster situations, and TAA benefits are payable only after regular UI benefits are exhausted for qualified claimants

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[19] This section relies on O'Leary (2011).

[20] States could choose two of the following four options: 1) UI eligibility while seeking only part-time work, 2) UI eligibility after job separations due to harassment or compelling family reasons, 3) continuation of UI benefits for at least 26 additional weeks after exhaustion of regular benefits while in approved training, and 4) dependents' allowances of at least $15 per dependent up to $50.

[21] For example, in 2013, Tennessee repealed a UI dependents allowance that was included in state legislation signed into law on June 25, 2009. In 2009, the U.S. Department of Labor issued Tennessee a $47.3 million payment for having an alternate base period and $94.5 million for having a dependents allowance and permitting UI eligibility for claimants who customarily held part-time jobs.

who lose their jobs due to trade.

If the President of the United States declares a disaster area, DUA is available to any unemployed worker or self-employed individual who lived, worked, or was scheduled to work in the disaster area at the time of the disaster, and who, because of the disaster, is struggling with one of four situations: the person 1) no longer has a job or a place to work, 2) cannot reach the place of work, 3) cannot work because of damage to the place of work, or 4) cannot work because of an injury caused by the disaster.[22]

The Trade Adjustment Assistance (TAA) program was enacted in 1974, and a series of program revisions have followed—the most recent occurring in 2015 (U.S. Department of Labor, undated 2). TAA provides extended income replacement payments to trade-affected unemployed workers who have exhausted their 26 weeks of regular UI benefits.[23] Current potential durations of TAA unemployment benefits are 130 weeks for eligible displaced worker enrolled in full-time training and by up to 156 weeks if remedial training is also necessary. TAA also pays the direct costs of job-skill training. Through 2019, a 72.5 percent tax credit against health insurance premiums is also available to TAA beneficiaries under the Health Coverage Tax Credit.

7. A European Unemployment Benefits Scheme

In this section we provide some background on existing UI programs in European countries. We also highlight the current proposals for the design of an EUBS, as well as the main concerns that have been raised by academics, policy-makers, and social partners about such a multinational system.

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[22] Most of this paragraph was drawn from http://www.ows.doleta.gov/unemploy/disaster.asp.

[23] The Trade Adjustment Assistance (TAA) program was created by the Trade Expansion Act of 1962 (P.L. 87-794) and was substantially modified by the Trade Act of 1974 (P.L. 93-618). NAFTA's Transitional Adjustment Assistance program (NAFTA-TAA) was created by the North American Free Trade Agreement Implementation Act (P.L. 103-182).

7.1. Background on Unemployment Insurance in European Countries

The onset of the 2008 global financial crisis quickly focused European policy-makers on UI (Beblavý and Lenaerts, 2017). Interest in UI redoubled during the Eurozone debt crisis of 2010. It became clear to many observers that the national policy instruments to prevent and/or absorb economic shocks were insufficient for dealing with the crisis and its consequences. EMU countries were unable to overcome the constraints of being in a currency union. For example, exchange rate and price devaluations were no longer available as policy instruments. This issue was further aggravated by the lack of supranational macroeconomic policy instruments, owing to the fact that EMU is not a fiscal union. Unemployment skyrocketed, and member states increasingly struggled to pay off or refinance their government debt. In an attempt to reduce costs, several member states scaled back their UI systems, for example by tightening eligibility rules, or by reducing the duration or level of benefits[24] – this occurred even after some member states had done exactly the opposite in the initial phases of the crisis. Next to unemployment, poverty became a severe issue in a number of member states.

The starting point for a European unemployment benefits scheme is very different from that in the United States (Beblavý and Lenaerts, 2017). All EU member states have unemployment benefits schemes, though some of these schemes are (much) more developed than others. In the EU, introducing an EUBS would thus, in practice, imply adding a supranational layer on top of these already existing schemes (that may fully or partially replace the existing national schemes). Like in the United States, member states' unemployment benefits schemes are tailored to the economic, cultural, and institutional circumstances of each member state. Thus, the existing schemes are highly diverse, in terms of their design, interlinkages with other

[24] Spain, for example, reduced the replacement rate in 2012.

(segments of) social insurance schemes, and objectives, among other features. As a result, imposing minimum standards that all national schemes would have to meet can be expected to present a major challenge in the European context. For example, the benefit amount is generally determined on the basis of a replacement rate, reference wage, and capping (sometimes other factors are considered, such as household composition or unemployment duration), but four countries – Ireland, Malta, Poland, and the UK – offer flat-rate benefits. Another example is the variation in the maximum duration of benefits, which ranges from just a few weeks to indefinite in Belgium. Furthermore, especially from the political point of view, there is much objection to interference from the EU level in domains that are still national responsibilities, with labor and social policies being a well-known example. In addition, while the introduction of a European unemployment benefits scheme will undoubtedly cause debate on what will happen to the existing state-level schemes, the role of the EU will also be subject to considerable discussion. Again, with regard to the latter, the vast differences in political views across the EU member states will come into play.

Another important distinction between the American and the European cases is that the motivations for introducing a multi-tiered UI system are different. In the EU, a two-tier unemployment benefits scheme has been discussed as an instrument to complete the EMU: a fiscal instrument that serves as an automatic, supranational stabilization mechanism that would help absorb economic shocks (European Commission, 2017c). The EUBS, as such, is inspired by the experiences of the member states that have shown that UI schemes are effective shock absorption instruments. Whereas social partners, in particular, are reflecting on whether an

EUBS could also function as a social instrument, in that way contributing to the European Pillar of Social Rights[25], but this consideration has not been taken up at the policy level.

Besides an EUBS, other stabilization mechanisms have been put forward in Europe. Some have been welcomed while others have been ignored, but to date there is no consensus on what approach would be most advantageous. The most commonly discussed alternatives are mechanisms linked to changes in GDP.

Despite the challenges ahead, the idea of setting up a European unemployment benefits scheme has received much attention recently. Especially after the Great Recession, when unemployment rates in Europe stood at record highs, it has gained momentum. Yet, when the crisis was ongoing, creating an EUBS was not a priority. Moreover, despite the urgency, the feasibility of launching such a scheme when unemployment levels are very high was questioned. Instead, the EU's governance framework underwent several other major changes. In the beginning of the crisis, most attention centered on the financial sector, which resulted in stricter monitoring and the Outright Monetary Transactions program of the European Central Bank.[26] At

[25] The European Pillar of Social Rights was first announced by the President of the European Commission, Jean-Claude Juncker during his State of the Union address of September 2015 and adopted in the Spring of 2017. With the Social Pillar, as it is also commonly referred to, the Commission aspires to increase the efforts towards fair and well-functioning labor markets and welfare systems in Europe. To be more precise, the European Pillar of Social Rights is a legal reference document that sets out 20 key principles and value shared across the Union. The Pillar has three main categories: 1) equal opportunities and access to the labor market, 2) fair working conditions, and 3) social protection and inclusion. As such, the Pillar serves as a framework that supports the monitoring of employment and social performance in the EU. As part of the third category, social protection and inclusion, the European Pillar of Social Rights stipulates that *"the unemployed have the right to adequate activation support from public employment services to (re)integrate in the labor market and adequate unemployment benefits of reasonable duration, in line with their contributions and national eligibility rules. Such benefit shall not constitute a disincentive for a quick return to employment"*. In this light, a European unemployment benefits scheme, through its design or the minimum standards it imposes, can have an important contribution. In addition to this argument, Beblavý and Lenaerts (2017) argue that the EUBS could help promote and develop the European Pillar of Social Rights through its effects on poverty and social cohesion, labor mobility, and by setting minimum standards that the Member States are obliged to meet in terms of the quality of their benefits system (e.g. in terms of level and duration of benefits) and activation policies.

[26] The Outright Monetary Transactions program allows the European Central Bank to make purchases in secondary, sovereign bond markets of bonds that are issued by the Member States of the Eurozone and mature in 1-3 years when a Member State ask financial assistance. This is only done when the Member State agrees to implement specific economic measures.

a later stage, the focus shifted to debt and investment, with the creation of the European Stability Mechanism as a prime example.[27] In response to the economic and social consequences of the crisis, the EUBS was not seen as a preferred solution.

While introducing an EUBS was not a priority at the time, the debate on this topic has made great progress over the same period. In 2012, the Four Presidents' Report entitled "Towards a Genuine Economic and Monetary Union" called for an EUBS (Van Rompuy et al., 2012). This idea has been advocated especially by then Commissioner for Employment, Social Affairs, and Inclusion, László Andor. In the subsequent Five Presidents' Report, the EUBS was not mentioned explicitly, but the ambition to complete the EMU by establishing a supranational automatic stabilizer was confirmed (Juncker et al., 2014). This is one of the four fronts on which the European Commission aspired to make progress towards a complete EMU by 2025. What is particularly interesting about both the Four Presidents' Report and the Five Presidents' Report is that each refers to the policy toolbox of other monetary unions across the globe – most notably the United States. In completing EMU, the EU hopes to draw lessons from their experiences.

In a more recent series of high-level EU reports, the notion of a shared unemployment benefits mechanism again resurfaced. On 1 March 2017, the European Commission issued its "White Paper of the Future of Europe," which outlined possible paths for the future of the EU by means of five scenarios (European Commission, 2017a). In the White Paper, the challenges to the Union's future, in the form of globalization, security, populism, and technological change, are addressed. As a follow-up to the White Paper, five reports on different topics were prepared. The first report in this series was the reflection paper on the social dimension of Europe, which highlighted the rights of citizens and workers in the Union and its relation to the European Pillar

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[27] The European Stability Mechanism is an intergovernmental organization that aims to safeguard and provide access to financial assistance programs for EMU Member States in financial need.

of Social Rights – but it did not make reference to the EUBS (European Commission, 2017b). The reflection paper on the deepening of the economic and monetary union, which was published a few months later, did touch on the topic (as before, it is listed as an option for a stabilization function) (European Commission, 2017c); in that paper, however, the EUBS takes the form of a European unemployment reinsurance scheme that would act as a "reinsurance fund" for the national unemployment insurance systems. More specifically, it would provide support to the national schemes in times of hardship, to ensure that the take-up of benefits remains high when resources are constrained.

Yet, notwithstanding these recent developments, the debate on a common European unemployment benefits scheme is not new. It dates back to the 1970s, when a number of reports were published that reflected on the future of Europe and what shape this could take. One of the earliest reports to take up the idea was the Marjolin et al. (1975) report. Around the same time, MacDougall et al. (1977) discussed the concept. After this initial episode, the debate languished until the late 1980s and early 1990s, when the topic was picked up again by Padoa-Schioppa et al. (1987) and Emerson et al. (1990). A range of proposals was put forward, but none were implemented. This lack of implementation is due to several reasons, including the full Maastricht Treaty agenda (there were many important topics on the agenda and a risk that not all countries would ratify the Treaty, and an EUBS was not seen as a priority), disagreements on the size of the EU budget and the upcoming enlargement of the Union (Beblavý, Marconi and Maselli, 2015). Perhaps even more importantly, at the time there was a widespread belief that asymmetric shocks would become rarer in a monetary union (Allard et al., 2003). As the Great Recession has clearly disproven this thesis, the issue of a supranational, automatic stabilizer and the notion that this could take the form of an EUBS are back on the agenda.

Whereas the positive economic and social effects of unemployment insurance at the member state level have been fundamental in encouraging the debate, the US two-tier UI model has consistently served as a guiding example of how an EUBS could be designed and implemented.

7.2. Design of a European unemployment benefits scheme

In the EU, there are currently no supranational unemployment benefits mechanisms, which means there is an array of options when it comes to designing an EUBS. Drawing inspiration from the UI systems of the member states and those found in other regions around the world, an EUBS could be composed of a range of features. For example, the duration of unemployment benefit pay-outs and the replacement rate exist in functional programs at the member state level (e.g. duration and level of benefits), other features could be unique to the supranational level. Mechanisms like experience rating of employer taxes or benefits drawn by frequent users could be specified or regulated at the supranational level.[28]

Although different options for an EUBS have indeed been explored in the academic and policy literature, these can generally be divided into two types: “genuine” EUBS and “equivalent” or “reinsurance” EUBS (Beblavý and Lenaerts, 2017). Genuine unemployment benefits schemes work in a similar way to the existing national schemes: they collect contributions directly from the individual employers, employees, or both and pay benefits directly to the unemployed.[29] The second group, the equivalent or reinsurance schemes, in

[28] Experience rating of employer taxes is only done in the U.S., while experience rating of benefit payments–known as a claw-back–was tried in Canada, but later repealed.

[29] Genuine UI schemes can be financed through contributions from employers, employees or both, which are determined as a percentage of the gross salary to be paid each month (Beblavý and Lenaerts, 2017).

contrast, would collect and distribute funds from and to the Member State level (and the Member States are then expected to use these funds to support the unemployed).[30]

Both types of schemes can function continuously or become activated (triggered), though reinsurance EUBS are generally designed to have a trigger as they are typically regarded as schemes that only come into play in the case of a severe economic downturn.[31] Both have their merits and drawbacks. For example, genuine schemes are more visible for citizens but also more difficult to implement; and vice versa for the reinsurance schemes.

Regardless of the type, a European unemployment benefits scheme is commonly designed with similar features as the member states' schemes. For example, an EUBS typically comes with eligibility conditions, criteria on the benefits that are paid out (e.g. duration, level, capping), financing rules, etc. The most comprehensive work on EUBS design is summarized by Beblavý and Lenaerts (2017), who describe the findings of a study of 18 potential schemes in a study that was carried out for the Directorate-General for Employment, Social Affairs, and Inclusion of the European Commission.

In that study, the level of unemployment benefits is determined on the basis of three parameters: the reference wage (i.e. the last gross monthly wage), the replacement rate (i.e. 35%, 50%, or 60% of the reference wage) and the maximum monthly benefit amount (i.e. 50%, 100% or 150% of the national average wage). In general, when compared to the unemployment benefits granted by the Member States' schemes, the EUBS in this study were quite generous. Other studies had suggested different values for these three parameters (but most used a similar

[30] Reinsurance UI schemes can be financed by means of a contribution to be paid by the Member States, for example a certain percentage of their GDP. In the study described in Beblavý and Lenaerts (2017), reinsurance schemes are financed through a start-stop mechanism: Member States pay into the EUBS until a certain amount of funds is reached (0.5% of EU GDP). Then, contributions are stopped until the EUBS' resources decline below this cut-off level, and so on.

[31] Dullien (2007), for instance, does propose a genuine EUBS with a trigger.

approach to determine the benefit level). Dullien (2007), for example, used a cap of 50% of the national wage as a default rather than the 150% as in Beblavý and Lenaerts (2017). Krueger and Muller (2010) recommended using a replacement rate of 50% as well. The benefit duration was set at 9 months (from the start of the fourth month until the end of the twelfth month of unemployment), with variations of 3 months (from month four to month six) and 12 months (from the first to the twelfth month of unemployment) – which is in line with the duration in most national schemes. A waiting period, however, results in a lower stabilization capacity and is therefore recommended against (Beblavý and Lenaerts, 2017).

In the work of Beblavý and Lenaerts (2017), any unemployed individual who has worked for three out of the last twelve months (3 months out of the last 6, or 12 months out of the last 24 being alternatives) is eligible for EUBS benefits. Other factors that are commonly considered to determine eligibility at the member state level, such as previous employment record, the nature of unemployment, or family status, are not taken into account for the EUBS. Dullien (2012; 2013) and Beblavý and Maselli (2014) used similar approaches. Note that there is ample diversity across the EU Member States in how eligibility for unemployment benefits is assessed. This is one of the areas in which matching the EUBS and the national schemes would be most challenging.

Considering that the EUBS would serve as a crisis intervention mechanism, the idea of allowing policy-makers to prolong the duration of EUBS benefits at times of very serious economic downturns has gained ground (Dullien, 2007; Beblavý, Gros and Maselli, 2015; Beblavý and Lenaerts, 2017). This idea is inspired by the US system of extended and emergency benefits, which proved to be highly effective in stabilization terms (Whittaker and Isaacs, 2014).

What has not been discussed very much in the EU is what is expected of the unemployed individuals receiving the European unemployment benefits in terms of availability for work, participation in active labor market policies, and related topics. These issues are often considered to be left to the discretion of the member states. While it may seem surprising that such important issues are not much discussed, the reason behind this is that the EUBS topic has mostly been approached from the EU level (i.e. studies have set out to understand what the supranational level could look like and how it would function and interact with the national UI schemes). In other words, primarily the role of the higher tier in the two-tier system has been analyzed.

7.3. Commonly discussed issues and concerns

Regardless of the design of a European unemployment benefits scheme, there are a number of issues and concerns that are at the forefront of the academic and policy debate. These are related to permanent transfers, moral hazard, the stabilization capacity of the scheme and the implementation of the scheme (Beblavý and Lenaerts, 2017).

The risk of giving rise to permanent transfers between EU member states is one of the main challenges to its introduction. Especially politically, this is a serious cause of concern. Considering that at the height of the crisis some (mainly Southern and Eastern) member states sought assistance from the EU and IMF to finance their debts, other member state governments were reluctant to provide resources out of fear for the political backlash they might face from their own voters. Bailing-out other member states while at the same time implementing unpopular policy measures (e.g. budget cuts), indeed, may be difficult to explain to national voters. In contrast to the United States, many EU citizens do not have a strong European identify, but rather a national identify (e.g. results from a 2014 Eurobarometer survey suggest that 40% of

EU citizens do not feel European) (Eurobarometer, 2014). As a result, in the EU cross-state solidarity and redistribution may raise more difficulties than in the US case. However, the survey results obtained by Vandenbroucke et al. (2018), suggesting that a majority of EU citizens would support modest transfers between countries, shed new light on this issue.

Nevertheless, as the EUBS is an insurance mechanism, transfers between the member states are unavoidable. However, it is often argued that long-run fiscal neutrality vis-à-vis the scheme is needed to prevent having some member states become permanent net contributors or recipients. From the political point of view in particular, the existence of permanent transfers would institute a barrier that is very difficult to overcome. This concern, however, can be addressed in the design of the EUBS. Mechanisms like experience rating and claw-back[32] are helpful in this regard, as both connect the pay-out received from the EUBS to the pay-in into the scheme. As explained in Beblavý and Lenaerts (2017), these two mechanisms are effective in achieving their objective: the simulations carried out show that no member state would be a permanent net recipient or contributor if a sufficiently long period is considered. Moreover, an EUBS is linked to short-term rather than long-term unemployment rates (i.e. it is insurance against cyclical not structural unemployment).

Closely related to the concerns about permanent transfers and redistribution, the issue of (institutional) moral hazard has also received considerable attention at the policy level (Claeys et al., 2014; Eichhorst and Wozny, 2014). Within the EUBS framework, institutional moral hazard may occur when the financing of the scheme and the payment of benefits remains at one level (the supranational level), while the implementation of the scheme and activation policies lies at

[32] Experience rating is a mechanism that links pay-in to pay-out by increasing the pay-in for Member States that use the EUBS more or that have a higher probability of doing so (e.g. higher unemployment rates on average). Claw-back is a mechanism that serves a similar purpose, but achieves this ex post, i.e. when Member States start building up a deficit vis-à-vis the EUBS that surpasses a certain cut-off level.

another (the state level). In such circumstances, the behavior of the lower level can affect outcomes at the higher level of government. In other words, member states can attempt to "game the system," with a view to gain as many resources from the EU level as possible.[33] Similar to permanent transfers, the issue of institutional moral hazard can be tackled in the design of the EUBS. By creating a scheme with experience rating, claw-back, and/or a trigger, as well as minimum standards setting how the funds provided by the EUBS are to be spent, moral hazard problems can be reduced. Although there are many ways to address institutional moral hazard (as demonstrated in a series of case studies by Vandenbroucke and Luigjes (2015), who also point to examples as financial incentives and conditional funding), it has to be acknowledged that a certain degree of moral hazard cannot be avoided. It is intrinsic to unemployment insurance. Moreover, this risk has to be weighed against the benefits that insurance brings.

These concerns about moral hazard and permanent transfers have to be seen in relation to the stabilization capacity of the EUBS: does the scheme deliver as a macroeconomic automatic stabilizer? The answer to this question fully depends on the design of the scheme, which implies, first of all, that any assessment of the scheme's stabilization capacity is based on assumptions of what the EUBS could look like as such a scheme is currently not in place, and secondly, that it is impossible to make any generalizations about the stabilization properties of an EUBS because it could take some many different forms (Eichhorst and Wozny, 2014; Gros, 2016). In addition, the stabilization capacity of the EUBS would need to be considered along two axes: spatial, i.e. reallocation of resources across member states within the same time period, to absorb

[33] Note that, in any unemployment insurance setting, there is also a risk of moral hazard at the level of the individual. This risk, however, is much less discussed in the EUBS debate, given that the national unemployment benefits schemes stay in place, at least partially (depending on the design of the EUBS). Eichhorst and Wozny (2014), moreover, suggest that the risk of individual moral hazard is reduced at the time of a crisis, when the EUBS would come into play.

asymmetric shocks, and inter-temporal, i.e. the reallocation of resources across time, to absorb symmetric or extended shocks (Dolls et al., 2014; Gros, 2016).[34] Again, the EUBS can be designed so that it would work on one of both of these axes, with major implications for its stabilization capacity.

That being said, previous research has produced estimates on the stabilization properties of the EUBS. Beblavý and Lenaerts (2017) summarize the results of backward- and forward-looking simulations of 18 EUBS. Although their conclusion is that the stabilization capacity of the EUBS is quite limited (i.e. only partial shock absorption), this results from the small scale of the additional unemployment benefit spending (i.e. the small size of the schemer). Another major conclusion of the study is that the reinsurance schemes have a higher stabilization capacity than the genuine schemes, the reason being that reinsurance schemes are focused on crisis years and the stabilization impact is highest at the start of the downturn. Reinsurance schemes with the lowest thresholds to be activated or triggered, moreover, have the largest stabilization impact on GDP.[35] On average, across the 18 schemes examined, the scale of the EUBS, measured as the total value of benefits paid out over 1995-2013 as a share of EA19 GDP, ranges from 0.03% to 0.43% of GDP. In 2009, the trough of the recession, GDP in the EA-19 would have been up to 0.2% higher if an EUBS had been in place. In an earlier publication, Dolls et al. (2014), using similar estimation techniques and EU-SILC data, compared a basic EUBS[36] with variants of this scheme (e.g. waiting period, more / less generous, equipped with experience rating or claw-back, etc.). Dolls et al. (2014) find that this basic scheme would have absorbed 36% of the

[34] Next to these two axes or channels, an EUBS could enhance existing national unemployment insurance schemes, in that way encouraging their counter-cyclicality (Beblavý and Lenaerts, 2017).

[35] There are many approaches as to how this trigger can be modelled. While generally the trigger and threshold are determined on the basis of the unemployment rates, Eichhorst and Wozny (2014) propose a model with a trigger linked to interest rates.

[36] This scheme has a replacement rate of 50 percent, a maximum duration of benefit receipt of 12 months and a broad coverage of all new unemployed with previous employment income.

unemployment shock in 2009 at the EA-level, while amounting to €49 billion per year. This amount could be financed by a contribution rate of 1.57% on employment income. Under this scenario, 5 EA member states would have been net permanent contributors or recipients of the EUBS. Although experience-rating claw-back mechanisms would be effective in preventing this outcome, this would reduce the stabilization impact of the scheme. Next to the work by Dolls et a. (2014), several other authors have provided estimations on the EUBS' stabilization capacity. Brandolini et al. (2016), for example, use data from the European Labour Force Survey for period 2002-12 to design a Notional Euro-wide Unemployment Insurance with 72 variants that is similar to reinsurance schemes proposed in other work. These 72 variants differ from each other in terms of coverage, replacement rate, duration, trigger and experience-rating. For each of these 72 variants, Brandolini et al. (2016) estimate the reduction in GDP volatility and the extent of cross-country redistribution. They find that the stabilization of the scheme with fill experience-rating would be between one-thirtieth and one-seventh of that provided by the current stabilization mechanisms. Depending on the design and the size of the scheme, the stabilization capacity of an EUBS could, therefore, be low to significant.

A final major discussion point relates to the implementation of the scheme (Beblavý and Lenaerts, 2017). Considering that the existing national unemployment benefits schemes are highly heterogeneous, in terms of scope, design, and other features, adding a European layer, especially in the form of a genuine EUBS, would be very complicated in legal, operational, and political terms. This is reflected in two ways: on the one hand, it becomes clear in how the EUBS and the national scheme would interact (e.g. if the EUBS benefit level is determined on the basis of the gross wage and the benefit given by the national scheme is a flat-rated amount, this might cause issues at the administrative and operational level). The adoption of an EUBS would go hand-in-hand with amendments in ordinary legislation on unemployment insurance, social security and social assistance, labor markets, and taxation in most member states. In administrative and operational terms, challenges would emerge as well (e.g. for data exchange between the different level, staff needed, etc.).

On the other hand, it also implies that if a harmonization of the national unemployment benefits schemes would be required, it would require large modifications in the national schemes. Such a harmonization would thus pose major challenges. Yet, harmonization is important to secure the stabilization capacity of the scheme (e.g. imposing a sufficiently long minimum duration of unemployment benefits is necessary as this is important for the capacity of the scheme to absorb shocks). A harmonization of the national schemes becomes more complex, the more different the former are from the European scheme. Furthermore, an unemployment insurance scheme also interacts with other dimensions of labor and social policies, which raises questions on how such interactions would be handled. In political terms, harmonization would lead to restrictions at the member state level as to how the national schemes would need to be designed and managed, as well as accountability issues.

Another aspect of the implementation relates to the role of social partners, which especially in a European context should not be overlooked (Claeys et al. 2014, Beblavý and Lenaerts 2017). In most EU member states, social partners are heavily involved in the design and management of the national unemployment benefits scheme. For example, employer representatives and trade unions can be involved in the monitoring of the NUBS or take part in discussions about its features. In some cases, for example Belgium, trade unions co-manage the national unemployment benefits scheme and can pay out unemployment benefits to their members. Moreover, in most member states, social partners are involved in wage setting through collective bargaining. Ensuring the involvement of the EU level and national level social partners in the EUBS is, therefore, essential. What is interesting about the position of the social partners is that they are critical of the idea of introducing an EUBS, and particularly at the national level, have often refuted it altogether. There are a variety of reasons for this, from concerns about workers' rights to adequate social protection to a fear of losing bargaining power. Whatever the reasons may be, getting social partners on board is an important precondition for an EUBS.

7.4. Outlook for the future

Although there is currently no European unemployment insurance scheme, the EUBS, as a reinsurance scheme backing up the national unemployment benefits systems, is being given serious consideration as a potential stabilizer by EU level policy-makers. As the economy is in recovery and unemployment rates are in decline, the time could be right to introduce an EUBS. However, its future ultimately lies in the hands of the member states. Whereas some member states have advocated the EUBS, notably Italy (which even came up with its own proposal)[37], other member states are much less inclined to support the idea. The recent elections in France and Germany are expected to influence the debate, and so will the upcoming European Parliament elections. As the current European Commission is now in its last year in office, it seems likely that the debate on the EUBS will be continued by the next Commission. This debate can build on a wider evidence base than before, taking into account the knowledge gathered on the EU context as well as the lessons from other two-tier systems such as the US UI scheme.

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[37] Even more recently, however, a new proposal for an EUBS emerged and is currently under discussion, i.e. a German-Spanish proposal for a robust European Unemployment Insurance.

8. Lessons for a European Unemployment Benefits System

The United States has more than 80 years of experience operating a multi-tiered unemployment insurance system. As the EU considers developing its own multi-tiered unemployment insurance system, the US experience offers some useful insights for the EU to consider. Following is a discussion of possibilities.

8.1. Gradual Development

The current multi-tiered system in the United States differs significantly today from the structure in the 1930s. This is not surprising, of course, given the changes in technology, the economy, and the labor force. Indeed, if anything, we are surprised at how little the system has changed. Two areas where the system has evolved are discussed below—the federal rules for conformity and federal support for states to engage in activities to monitor claimant work-search activity. In addition, states themselves have modified their systems by adjusting benefit amounts and potential durations.

As described above, states are required to meet certain requirements for their UI system to be considered in conformity with federal law. Employers in states that fail to be in conformity do not receive the 90 percent FUTA tax reduction for employers, and the state does not receive federal payments for administrating the state UI system; thus, the conformity provisions include substantial financial pressures for states to meet them. The original UI legislation included 12 conformity provisions, and additional requirements have been added over time. The most recent additions have included federal eligibility requirements for extended benefits, requirements for states to establish profiling systems to identify and serve claimants likely to exhaust their benefits, and requirements for states to establish systems allowing beneficiaries to choose federal income-tax withholding. Interestingly, some of the US conformity changes have been rather minor, such as denying benefits to professional athletes in the off-season, while others, such as requiring state participation in the extended benefits program, have represented major changes to the system. In the United States, conformity requirements do not specify rules for setting wage replacement rates or maximum weekly benefit amounts, which as of January 2019 for individual states ranged from $240 in Arizona to $1,192 in Massachusetts including dependents allowances.

Another example of gradual change in the US system pertains to enhanced efforts to reduce UI payments through increased monitoring and reemployment services. Efforts in this area have included both mandatory activities and voluntary activities. In 1993, states were required to develop and implement Worker Profiling and Reemployment Services (WPRS) systems, which included the use of statistical profiling models to identify claimants likely to exhaust benefits, who were then targeted for mandatory reemployment services. In 2005, the Reemployment and Eligibility Assessment (REA) program was made available to states on a voluntary basis to provide a combination of enforcement actions (eligibility assessment) and reemployment services. The program started with 20 states in 2005, and it has grown to cover nearly all states. In 2015, the program was renamed Reemployment Services and Eligibility Assessments (RESEA), and virtually all states and other eligible entities now receive awards. Under RESEA, states are encouraged to use their WPRS statistical models to target RESEA services on those predicted to be most likely to exhaust benefits. During the Great Recession, all states received large grants to provide reemployment services (RES) to claimants, but these grants were one-time efforts and were not continued.

8.2. Approaches to Encouraging Lower-Tier Behavior

Much of the concern in a multi-tiered system involves principal-agent problems—efforts by the higher-level entity (the federal government) to get the lower tier (the states) to behave in accordance with the higher tier's wishes. The UI system in the United States has made use of a variety of approaches to influence state behavior: mandates, discretionary grants, and universal grants. The efforts to encourage work-test enforcement and provision of reemployment services to claimants show the mix of approaches that have been tried. The WPRS system instituted in 1993 added worker profiling and the provision of reemployment services to the conformity requirements, making any state that failed to implement the program subject to the loss of the 90 percent FUTA tax reduction. During the Great Recession, the American Recovery and Reinvestment Act of 2009 (ARRA) added $246.9 million for reemployment services for UI claimants, a significant sum compared to the regular Wagner-Peyser Act allocation of $701.9 million and the ARRA general supplement for Wagner-Peyser labor exchange activities of $148.1 million.[38] The REA program, now called RESEA, illustrates a third approach, whereby states are not required to undertake the activities but can apply for the funds to implement the program.

The lesson is that all three approaches can be effective, but they have different pros and cons. Mandating certain behavior is least expensive to the higher tier but may not be politically feasible, particularly if the lower-tier members have sovereignty and different preferences for policies. The universal funding approach is generally effective in getting the lower-tier members to implement the policy, but the cost to the higher tier is much higher. Finally, the voluntary approach is intermediate in terms of cost to the higher tier, but participation by the lower tier may be limited. This slower response can be advantageous, as in the case of REA/RESEA, where

[38] While the ARRA funding increases for reemployment services were large relative to baseline levels, it should be noted that U.S. funding for active labor-market programs remains far below levels sufficient to overcome the employment disincentives inherent in UI payment. Martin (2014) reports the average spending on active measures in OECD countries to be 0.65 percent of GDP, which he suggests is nearly sufficient to balance typically generous UI systems. However, the U.S. rate of spending on active measures is low. It was only 0.14 percent of GDP in 2011, a year of relatively high recession-level spending on active measures.

gradual implementation permitted states to try different approaches, and evaluations were conducted to provide more information on the effectiveness of REA/RESEA. The UI Modernization Act, passed during the Great Recession, offers another example of the use of financial incentives to encourage states to behave in a particular way; in the modernization program, states could obtain substantial federal funding by adopting specific policies designed to increase the population eligible for UI or provide additional benefits.

8.3. Financing Provisions

Financing of the US system is complex, and the structure has both advantages and disadvantages that should be considered by the EU. As was described in more detail above, funds for the UI program in the United States are primarily raised through payroll taxes on employers; the funds are sent to the federal government and most of the money returned to the states that meet conformity requirements. Funds for state administrative functions are financed from the 10 percent federal reserve of FUTA tax revenues. The US approach to UI financing may not be the right strategy for the EU, but it offers some interesting options, which are discussed below.

Payroll taxes have some attractive features for financing unemployment insurance. First, the payroll tax base corresponds well to the benefit principle of taxation, where those who benefit from a government service pay for the service. Second, permitting each state to set its own tax structure permits states to determine how generous their UI system should be while making states bear the consequences of the generosity of their UI benefits. Third, the procedure of relieving employers of 90 percent of the federal tax for conformity gives the federal government considerable leverage over the design of state programs—employers in states out of conformity would be subject to a payroll tax of 6.0 percent rather than 0.6 percent for the FUTA tax. The conformity requirement that states must use experience rating to set any employer's state UI tax rate below the FUTA level is an attractive financing feature, as it gives employers an incentive to make sure that claimants are in compliance with the separation requirements for UI eligibility. One essential principle is to balance benefits and financing. For example, if the maximum benefit amount is indexed to average earnings, then taxable wages should be indexed in a similar way to earnings. This principle of balancing system revenues and expenses should ensure fiscal integrity over business cycles.

There are, however, some financing features of the UI financing structure in the United States that the EU may not find appealing. For example, the FUTA tax base is only $7,000, making the tax regressive and providing an incentive for employers to favor high-wage workers in hiring decisions;[39] the low tax base can be justified, at least in part, because UI benefits are not based on all earnings—a sizable proportion of workers earn more than the UI taxable wage maximum. Another unusual feature of the US financing system is that the revenues are obtained through state taxes on employers, which then become part of the federal budget and are rebated to the states. This approach complicates the system and perhaps gives the false impression that the taxes raised by the states are federal in nature; an advantage of the current system is that it makes administration of the trust funds similar across states and facilitates the federal government's ability to make loans to states whose trust-fund balances are inadequate. A final feature of the US financing system that the EU may find troubling is that state administrative costs are distributed to states based on historical cost experience; this approach creates a moral

[39] Another regressive feature of the U.S. system is that the UI taxes are applied to the "person-job." Thus, a low-wage worker who holds two jobs would have more UI taxes paid in by employers for them than would a person with a higher wage rate but a single employer.

hazard whereby states can increase employee salaries and UI services without bearing the full cost.

8.4. Variations in State Provisions

The UI system in the United States permits large variations in state provisions regarding features on the benefits side, such as monetary and nonmonetary eligibility, work test enforcement, benefit size, and benefit duration. The EU might wish to consider the advantages and disadvantages of permitting such large differences. On the tax side, there are variations in the tax base, experience rating, and wages subject to the state payroll tax. As previously noted, for example, the maximum number of weeks of coverage has traditionally been 26, but in 2018, eight states had lower maximum weeks. There also is a very large range in weekly benefits, with the most generous state having maximum weekly benefits four times as high as the lowest state. On the tax side, the payroll tax base in 2018 was as low as $7,000 annually in three states (Arizona, California, and Florida) and as high as $47,300 in Washington State. State tax rates ranged from zero in many states up to 11.13 percent in Massachusetts in 2018.

Does it make sense to permit such large variation in taxes and benefits? The United States historically has allowed states to vary the generosity of assistance programs; for example, in 2018, the range in state benefits for the Temporary Assistance for Needy Families (TANF) welfare program for a family of three ranged from $170 per month in Mississippi to $1,039 in New Hampshire.[40] Large variations in assistance programs might encourage migration to high-payment states. The decision on whether to permit large variations in benefits depends on many

[40] TANF monthly benefit data are from the Center on Budget and Policy Priorities as of July 2018, https://www.cbpp.org/research/family-income-support/tanf-benefits-remain-low-despite-recent-increases-in-some-states retrieved April 21, 2019.

factors, including sovereignty of the second-tier entities as well as the extent to which the program is centrally funded.

8.5. Redistribution Issues

Redistribution of funds raised can occur within states and across states in the US system. The UI system includes little redistribution across states, as funds raised for UI benefits all come from employers within the state. The exception is for state administrative expenses, where funds are distributed based on historical state experience in staffing and salaries. Within states, there is a greater possibility for redistribution among employers, depending on how well a state's experience rating system corresponds to an employer's experience in laying off workers.

The advantage of the US approach is that each state decides how generous its benefits should be, but the state must be willing to raise enough funding to pay for the benefits. In contrast, the US welfare system includes a substantial amount of redistribution, where wealthier states are required to pay a greater share of program costs than poorer states.[41] A system with substantial redistribution introduces the possibility of "institutional moral hazard," where the second-tier entities have an incentive to provide more benefits than they would be willing to pay for (Vandenbroucke et al. 2016). The EU may wish to have some degree of redistribution—if not, the current system of independent national systems could be maintained.

8.6. Crisis Intervention

The United States has established two types of programs to deal with periods of very high unemployment. The extended benefits (EB) program has been in place since 1970; however, it has not been a functioning program in any significant way since 1980. The idea behind the EB

[41] The relationship between federal contributions and state income was clearer before 1997, when the Personal Responsibility and Work Opportunity Reconciliation Act (PRWORA) froze the federal contribution to the welfare program, TANF, as a block grant. Also, states with lower incomes tend to have lower benefits.

program is to have a permanent program in place that automatically goes into effect when there is unusually high unemployment. In practice, the EB program has proven to be politically unsustainable. It has been overwhelmed by a discretionary approach that is often used in times of generally high unemployment—i.e., enacting special legislation at the federal level to pay for longer-duration benefits. In the United States, these programs have typically been financed entirely by the federal government, which possibly explains why states have set the parameters of their EB programs so that they are never triggered. Woodbury and Rubin (1997) note there were only six temporary UI extensions between 1970 and 1995. In addition, an emergency program operated from 2002 to 2004 and another, involving several revisions, was adopted during the Great Recession.

The United States has opted to finance the temporary programs with general revenues. Because most states have balanced-budget requirements and the federal government does not, it would be difficult for states to mount new UI programs during a severe recession—a period when state government revenues are stagnant. The EU should consider whether crisis interventions should be implemented in advance—as the EB program in the United States is intended to operate—in an automatic way as crises develop, or as the US temporary discretionary EUC type programs have operated. Other issues to consider are which level or levels of taxation should pay for the program, what the triggering mechanisms would be for EB, and whether the crisis programs should involve changes in the definition of suitable work.

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